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## **Research on microfinance in India: combining impact assessment with a broader development perspective.**

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September 2011.

**Abstract:** *Microfinance can be researched narrowly as an instrument for promoting development or more broadly as an endogenous component of development. The paper sets out a simple well-being regime model incorporating both views and uses it to review the dynamics of rural microfinance in India. Four potential drivers of change in the role of microfinance in India are reviewed: evidence-based policy, rising political aspirations, new technology and agro-climatic change. The paper argues for combining more narrowly focused microfinance impact assessment with broader research into microfinance as one component of wider well-being regimes.*

**Key words:** development research, impact assessment, microfinance, rural development, well-being regimes, India.

### **1. Introduction**

This paper is motivated by ongoing debate over both the commercialization and what can provocatively be called the medicalization of microfinance. The first refers to the assumption (notwithstanding the 2008-9 financial crisis) that microfinance is inevitably becoming integrated into global financial markets, and the second to the growing popularity among agencies supporting microfinance of a normative medical metaphor for aid: namely, that ‘treatments’ such as microcredit should be applied to selected groups only on the basis of rigorous demonstration of their positive impact on measurable outcome indicators, preferably based on randomized control trials. While both perspectives have their merits, the fact that they take such strikingly different positions on the tension between structure and agency suggests a continued need to consider microfinance from other perspectives also.

To this end the paper first advocates reviewing the relationship between microfinance and development within a broad well-being regime framework. The argument is then developed through an unsystematic but wide-ranging survey of the secondary literature on rural microfinance in India.<sup>2</sup> The remainder of this

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<sup>1</sup> [j.g.copestake@bath.ac.uk](mailto:j.g.copestake@bath.ac.uk). This paper was first presented at a workshop in January 2010 organized by the Centre for Research into Microfinance in Brussels on microfinance and development studies. I am grateful to participants for comments, particularly Cyril Fouillet, and to Julie Humberstone for assistance in searching the literature.

<sup>2</sup> Some degree of order was introduced through a systematic search for abstracts that referred to (a) India or regions thereof (b) poverty or related concepts (c) microfinance or related instruments (d) impact or related concepts. This covered four databases (EconLit, IBSS, ISI Web of Knowledge and Business Source Premier) going back to 1991. Obvious flaws in this search strategy include omission of the rich literature on microfinance in India in languages other than English, and failure to pick up

section defines development as the adaptive evolution of national well-being regimes, of which microfinance is one component. Section 2 briefly applies the framework to India's recent history. Section 3 develops the analysis further by reviewing research into the relationship between rural microfinance and four potential drivers of change: evidence based policy, rising political aspirations, new information and communication technology (ICT), and food insecurity linked to climate change. Section 4 addresses implications for discussion of microfinance research priorities, concluding with a warning against policy-oriented impact assessment crowding out broader and more open-ended research.

The term microfinance is used to refer to institutions of saving, credit, insurance and money transfer used by relatively poor people. Most analysis of microfinance is framed as a micro-level issue, centered on the behavior of specific users and providers. However, such analysis is also unavoidably - if often implicitly - framed by a wider view of how the state, markets and society jointly determine the distribution of well-being and poverty. For example, public support for private microfinance institutions (MFIs) might be viewed both positively and negatively: for example, as a means to promoting financial inclusion by 'making markets work for the poor', or as political cover for state retreat from more comprehensive social insurance commitments. And both views are conceivably compatible with a "pluralist liberal orthodoxy" that seeks to identify the least worst combination of state, market and civic mechanisms for addressing poverty in countries where all three are deeply compromised by other political priorities and interests (Brett, 2009). Variation in such constraints over time and space creates path dependencies and limits the usefulness of evaluating particular financial mechanisms against any universal theory of development.

One way to contextualize analysis of microfinance is to view it as part of an evolving national well-being regime. This approach can be traced back to classical political economy, refashioned through comparative social policy, particularly under the influence of Polanyi and Esping-Anderson (Gough & Wood, 2004). The main emphasis in this paper is on well-being regimes at the national level, though there is potential to extend the analysis at global and sub-national levels also. The broad framework is captured in its simplest form by Figure 1. This depicts a feedback loop whereby from any given starting point (determined by an endowment of exogenous conditioning factors) an institutional matrix of state, market, civil society (including community) and household mechanisms distribute resources in such a way as to determine the distribution of well-being outcomes across the population.<sup>3</sup>

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anthropological research that touches on microfinance indirectly as one element of agrarian social relations. The paper also predates the 2010 'crisis' of microfinance in Andhra Pradesh, which further illustrates the central argument in favour of broadening the framework of analysis of how microfinance relates to development.

<sup>3</sup> Drawing on Powelson (1997) as well as North (1990), the term institution is taken to refer to rules and norms governing resource allocation that are protected by culture, in the sense that non-compliance with them provokes widespread outrage and a political

Well-being is defined broadly to include human capabilities, opportunities and emotional states including life, liberty and happiness.<sup>4</sup> The term is used in preference to 'welfare' to signal a break with the assumption that individuals operate solely on the basis of material self-interest and that institutions persist solely as a consequence of their functional contribution to individual and collective material interests. This is not to deny the power of such political economy perspectives, but to acknowledge the importance of other social processes, including the politics of identity and recognition. One further clarification is that notwithstanding use of the term well-being, the framework aims primarily to inform positive rather than normative analysis; thus a particular well-being regime may more appropriately be referred to as an insecurity regime, for example.<sup>5</sup>

A given well-being outcome triggers a set of reproduction consequences. These include changes in wealth, power, perception and capacity of different groups for collective action to alter the institutional matrix, and hence future well-being outcomes through processes of cumulative causation. Outcomes may also have deeper effects on the conditioning factors underpinning the institutional matrix. However, implicit in the idea of a 'regime' is the assumption that radical system change or breakdown is an exception to the norm. For example, business and political cycles along with deeper fluctuations in the balance of power between state, market and civil society do not amount of themselves to regime change if they trigger 'corrective' feedback.

One possible use of this framework is to assess the systemic role of specific components of the institutional matrix. If a particular institution, such as rural debt, persists over time then this suggests it plays a role in overall regime stability, and it is useful to understand how, as well as why attempts to change it are likely to be resisted. Its role can then be further explored by appraising how it will be affected by exogenous shocks.

Potential well-being outcomes of microfinance include capacity to save, to take and spread risks, to smooth consumption, to meet lumpy expenditure needs and investment opportunities, and to make and receive transfers easily (Collins *et al.*, 2009). Technical change that improves access to such services by lowering transactions costs can enhance these outcomes. If users experience reduced vulnerability and are able to accumulate assets then this has potentially benign expanded reproduction possibilities, including a virtuous cycle of financial inclusion as poor people raise their debt-capacity and this in turn reduces unit costs of microfinance even further.

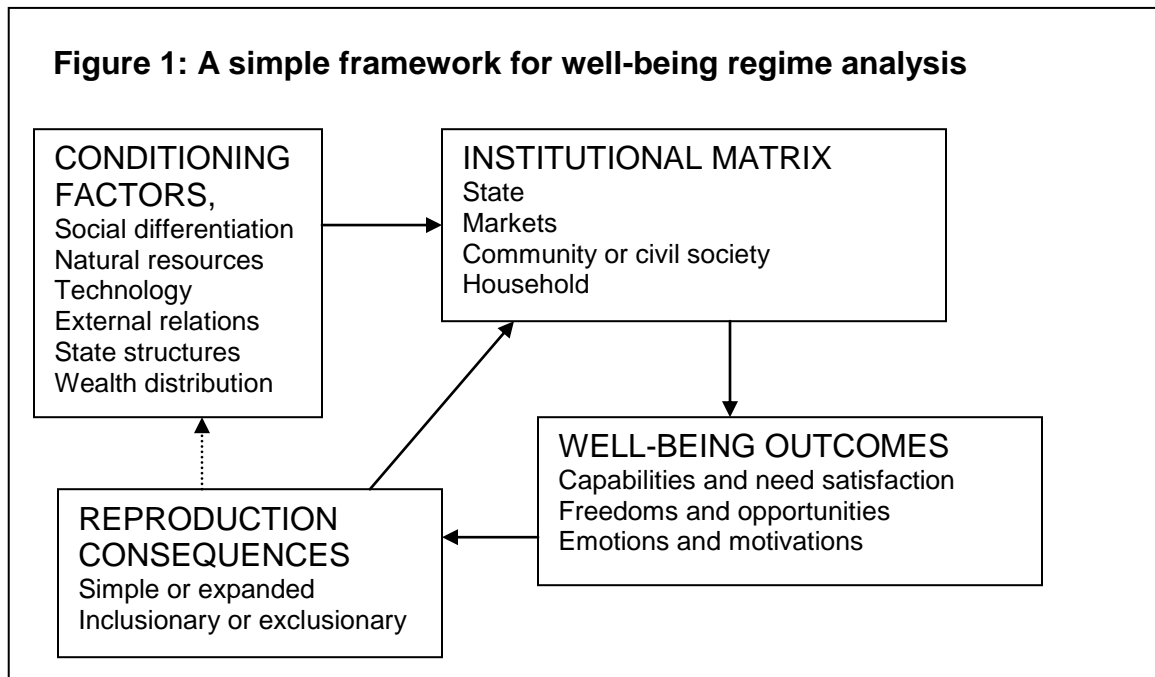
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reaction in their defence. The framework can be elaborated further by incorporating Williamson's (2000) distinction between four levels of institutions.

<sup>4</sup> This echoes the Wellbeing in Developing Countries (WeD) network definition of well-being as "a state of being in society where people's basic needs are met, where they can act effectively and meaningfully in pursuit of their goals and where they feel satisfied with their life" (Copestake, 2008:3).

<sup>5</sup> For other examples, see Bevan in Gough & Wood (2004) on in/security regimes in Africa, and Copestake & Wood in Copestake (2008) on Peru as an unequal security regime.

Conversely, access to financial services only on the most adverse terms can foster over-indebtedness, dependency, poverty and low aspirations. It is implicit in the definition of microfinance that access to finance is segmented by income, whether because technology is not scale-neutral or because poorer users face discrimination. In short, microfinance can also play a key role in the reproduction of inequality. On the supply side, unequal ownership and control of microfinance services can also contribute to the reproduction of poverty and inequality.



More radical feedback loops are possible via the conditioning factors governing finance, including generalized trust across markets and the influence on economic growth of the institutions governing creditor risk (Fergusson, 2006). The distributional consequences are again important, such as whether improved governance at the top end of the financial market has positive spillover effects on lower market segments or reinforces institutional dualism (Figueroa, 2009).

This analysis highlights potential dangers of separating analysis of services for the poor from those available for the rich. Too strong a focus on individual access to microfinance risks contributing to neglect of financing collective needs of poor people, including physical infrastructure, security, health and education services. At worst, it can be a smokescreen for deeper structural forces, and sustain overly simplistic rhetoric of equality of opportunity. These arguments help to explain why social scientists have treated donor interest in financial inclusion cautiously (Fernando, 2006; Weber, 2004). At the same time a broad-brush sectoral view of development finance risks reducing the focus on poverty and distribution (Johnson, 2009).

A second possible danger arising from an overly narrow focus on microfinance is that it neglects the way differentiated access to financial services is interlinked with other components of the institutional matrix. A potential advantage of microfinance is that it frees individual users to make use of improved liquidity as they see fit. Likewise the shift from solidarity based peer-lending mechanisms to more flexible and open-ended individual lending is more likely to be beneficial by reducing loan transaction costs and thereby facilitating scaling-up. However, this neglects evidence of the resilience of interlinkage between microfinance and other services, as well as the rationale for more radical strategies for poverty reduction that rely on combining financial and other interventions.

Linked to this is the trend towards downplaying the spatial segmentation of microfinance. Rural urbanization, increased spatial mobility and improved communications all help to explain why location matters less than it used to for many people, and why models based on simple rural-urban or formal-informal dualities are misleading. But poverty remains overwhelmingly rural in many parts of the world, and villages a repository of deep geographical and cultural constraints to market intergration. The potential impact of microfinance may hinge less on the value of financial resources transferred than on their potential negative and positive impact on social relations underpinning poverty, including clientelism and capacity for collective action.

## **2. The case of India**

The previous section presented a simple framework for viewing microfinance as part of a broader historical-institutional analysis of development as the evolution of national well-being regimes. This section provides a brief worked example, comprising an historical overview of rural microfinance as one component of India's well-being regime.

My own first-hand experience of doing field work on rural credit in Tamil Nadu during the 1980s at times seemed to entail not just "reconstructing landscapes" (Bouman & Hospes, 1994) but also what might be called financial systems archeology. Each visit to a cramped primary agricultural credit cooperative, bank branch or half-empty government office revealed further corners of a labyrinth of financial initiatives: privileged conduits of new money lying over the clogged pipes of long neglected schemes. At the same time, I also marveled at the scale and resilience of some of these historic institutions: the survival from one government to next of the cooperative system as a conduit for short-term agricultural credit; the continued operation of remote branches of commercial banks and regional rural banks (RRBs), the perpetuation of IRDP as an instrument of central government patronage long after its launch in 1979 (Copestake, 1996), and the myriad shoe-string Gandhian programmes for supporting village industry and self-reliance.<sup>6</sup> Harder to unearth but equally

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<sup>6</sup> Despite chronic weaknesses, the short-term cooperative credit system still had 127 million members in 2005, including 45 million who received loans (Government of India, 2008:73). IRDP was rebranded as SGSY in 1999 and subsequently became a major

important to well-being outcomes were the pervasive root systems of informal money-lending and indebtedness (Shah *et al.*, 2007).

State sponsored rural credit was also only one component of a wider regime of public spending that also encompassed investment in infrastructure, a plethora of nutrition and employment creation schemes, and subsidized supply of electricity, food, fertilizer and other agricultural services. While debate raged over the strengths and weaknesses of rival schemes, criticism was also growing of the cost, inefficiency and perverse incentives to innovation of the whole rural subsidy regime. How far was this the product of a benign, if high-handed and paternalistic developmental state, and how far had it degenerated into a parasitical and often openly corrupt patronage system? With gloriously disingenuous hindsight, some commentators wrapped the whole experience of *dirigiste* social banking up with the 'licence raj', labelled it 'rent-seeking' and consigned it to the dustbin of history (e.g. Farrell and Lund, 2006). In contrast, more measured historical assessments confirmed significant positive links from rural bank branch and credit expansion to faster agricultural growth (Binswanger & Khandker, 1995) and poverty reduction (Burgess & Pande, 2005).

After the shock of the external crisis of 1991, and taking the Narisimham Committee report of that year as its blueprint, the BJP government did begin to restrict the flow of public credit to priority sectors and backward regions. But the number of rural bank branches, which peaked at 35,396 in 1993-94, still exceeded 30,000 in 2005-6; while the total number of loan accounts below Rs 25,000 fell from a peak of 63 million in 1991-2 to a trough of 37 million in 2003-4 before beginning to rise again (Pillarisetti, 2007:28-30). Debt outstanding with moneylenders, evident from successive rounds of the National Sample Survey, mirrored these changes (Pillarisetti, 2007:31). Other commentators provide a more thorough review (Ramachandran & Swaminathan, 2005; Shah *et al.*, 2007). While acknowledging that they were in part legitimized by the scale of corruption and waste associated with some regions and programmes (particularly IRDP/SGSY in the North and East) they argue that the reforms also reflected a political swing away from rural and farming constituencies in favour of the growing urban middle-class.<sup>7</sup>

In contrast, the victory of the United Progressive Alliance in May 2004 can be interpreted as a popular reaction against a thirteen year swing towards a market-led model of development. Since then there has been at least some public reaffirmation of the importance of both rural finance and public investment in rural infrastructure as part of a well-being regime focused on achieving social inclusion through a combination of increased democratic participation and

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source of funding for self-help groups. Rajasekhar (2006) reviews its coverage and operational weaknesses for the five years to 2003-4. On RRBs, see Kaushik (1996).

<sup>7</sup> More recently Chakraborty and Dasgupta (2010) describe the adverse effect of anti-inflationary sterilization of private capital inflows by the Reserve Bank of India on the supply of capital for rural lending via NABARD. The offsetting positive contribution of foreign capital inflows to rural microfinance via investment in MFIs is likely to have been much smaller.

“inclusive growth” (Thorat, 2008).<sup>8</sup> The Rangajaran report of the Committee on Financial Inclusion (GOI, 2008:42-44) set a target of providing “comprehensive financial services” by 2012 to 50 percent of the 65 million cultivator and 47 million non-cultivator households identified by the 2003 NSS study as lacking access to formal financial services.

An important link from pre-1991 to current credit policy has been the growth of the Self-Help Group (SHG) movement. This emerged during the 1980s, particularly in the Southern States and through the social intermediation of rural development oriented NGOs (Fisher, *et al.* 2002). The role of SHGs as intermediaries between individual clients - mostly women - and the banking system accelerated particularly after NABARD launched the National Self-Help Group Bank Linkage Program (SBLP) in 1992. In April 2001, 285,000 self-help groups (SHGs) had taken loans from commercial banks, regional rural banks and cooperative banks through NABARD’s self-help group-bank linkage program (SBLP). With an estimated average of 17 members per group, it could thereby claim to reach approximately 4.5 million people (Fisher, *et al.* 2002). By 2009, in contrast the number of people accessing formal credit and savings through SBLP had increased to 63.6 million, through 3.47 million SHGs (Sa-Dhan, 2009a:2; Srinivasan, 2008). The SBLP approach has been praised for its ability to increase outreach and described as India’s dominant mode of microfinance (Basu 2006). Financial support has not only been routed via banks under the SBLP but also through a rapid expansion in the number and size of specialized microfinance institutions (MFIs). By 2008, 233 MFIs reached 22.6 million clients independently of SBLP, with 62% of this outreach being accounted for by for-profit MFIs (Sa-Dhan, 2009b:ii).

However, rapid growth of lending through SHGs and MFIs has also generated a new set of challenges and concerns (Basu 2006; Sa-Dahn 2009a; Srinivasan 2008). Some MFIs promoting SHGs overstretched their management systems, and others with weaker management and governance also began to engage in SHG promotion. By transforming into for-profit entities in pursuit of faster growth some of the largest MFIs have also come under attack for abandoning the philosophy underpinning SHGs, neglecting the poorest and using public funds for personal enrichment (e.g. T.Nair, 2010; Sriram, 2010). Competition amongst microfinance organizations also increased, and in some areas this has resulted in multiple borrowing and over-indebtedness. In 2006, MFIs in Andhra Pradesh were accused by politicians and the media of charging usurious interest rates and of unethical debt collection techniques that contributed to the wave of suicides among indebted farmers. The MFIs in turn attacked state subsidies to SHGs, and the effect of debt forgiveness benefitting nearly 40 million farmers – a political response that signaled regime continuity between the SHG model as a modality of rural finance and many of the credit initiatives that preceded it.

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<sup>8</sup> In addition to the SBLP programme, discussed below, Thorat (2008:5) identifies the establishment of NABARD’s Rural Infrastructure Development Fund and the Small Industries Development Bank of India (SIDBI) as important initiatives taken in the 1990s to maintain the flow of development finance to agriculture and other priority sectors.



To sum up, state support for rural credit has been a significant and resilient component of India's well-being regime for fifty years, despite numerous changes in credit disbursement modalities and a sustained attempt to bring about market-oriented forms between 1991 and 2004. And if poverty rates did fall by as much as half a percent per year, as contested official statistics suggest (Pillarisetti, 2007:22), there are no reliable estimates of the contribution of state sponsored rural credit to this fall. Shah *et al.* (2007) suggest that the scale of the commitment to rural credit will indeed be seen with hindsight to have been modest and temporary against the backdrop of a century of chronic agrarian indebtedness, while the national surveys of rural indebtedness remind us that "the commercial money-lending firm remains key to the cycle of production" (Harriss-White, 2008:550).

The analysis of India's well-being regime could be further elaborated through a more detailed investigation not only of changes in the institutional matrix, well-being outcomes and reproduction consequences but also of the political processes regulating system change. Mooij (2007) points in this direction by noting a persistent need for central government to assert the importance of progressive social policies and its control over them, while at the same time lacking commitment to combat local subversion of their implementation at state level and below. Development schemes framed in the language of universal citizenship are distorted "...beyond all recognition in implementation such that although practical outcomes vary according to local balance of social and political forces, they tend to reinforce unequal citizenship." (Harris-White *et al.*, 2009:3). However, to the extent that financial and other forms of liberalization increase income polarization (by region, caste, class, ethnicity, gender) so the centre is constrained to retain its fiat on compromised mechanisms for disbursing regional patronage as a means to the reproduction of national unity.

### **3. Selected drivers of change in India**

Having provided a rough sketch of how rural microfinance in India fits into a well-being regime analysis, this section uses the framework to review more specific drivers of change. The first of these is the 'endogenous' process of deliberative reform of the institutional matrix in the light of research into the impact of its component parts. The implicit assumption here is that there is sufficient political room for manoeuvre to allow policy makers to make rational policy adjustments in the light of empirical evidence. We then turn to the relationship between rural microfinance and three 'exogenous' potential drivers of regime change: (a) rising popular aspirations and political responses to them; (b) organizational implications of new ICT; (c) food insecurity linked to climate change

### *Evidence based policy adjustment*

The main focus of recent impact research has been the SHG Bank-linkage programme. Among the many studies are those carried out by Deininger and Liu (2009), Swain and Varghese (2009), Swain and Wallentin (2009), Garikipati (2008), Sarkar and De (2005), Puhazhendi and Badatya (2002) and Puhazhendi and Satyasai (2001). These generally report some positive economic impact, though rarely sufficient to have a dramatic impact on poverty incidence. Few loans are used to set up new businesses (Gadenne & Vasudevan 2007; Kalpana 2008; Sa-Dhan, 2009b).<sup>9</sup> Instead they are mostly used either as working capital for existing household enterprises, to purchase livestock, or to manage consumption flows. Limited impact is variously associated with the small size of loans, lack of business opportunities and failure to complement microcredit with complementary inputs such as education, training and business development services. Most studies also report positive cognitive and attitudinal effects, including increased self-confidence, self-esteem and ability to deal with problems (e.g. Puhazhendi & Badatya 2002b; Fisher *et al.* 2002; Boraian, 2003; Holvoet, 2005b, 2006; Moyle *et al.* 2006; Bagheri *et al.*, 2007; Sinha 2008). Mohindra *et al.* (2008) also find positive effects of SHG membership on women's inclusion in health care and their mental health. However, evidence of significant and tangible positive effects on women's decision-making power, control over assets and participation in extra-household networks is less pronounced (Puhazhendi & Badatya 2002a; Holvoet, 2005a; Sinha 2006; Garikipati 2008; Banerjee *et al.* 2009).

SHGs supported and linked to banks by NGOs are generally found to perform better (in terms of targeting, social and economic impact, and repayment rates) than SHGs linked directly to banks or by government to banks (Swain & Varghese 2009b; Puhazhendi & Satyasai 2001), with government linked SHGs tending to perform the worst (Sinha 2008). However, the number of studies that systematically compare impact of for-profit MFIs and non-profit SHGs is surprisingly small given the extent to which differences in their ideology and approach drive policy discussion. Likewise, relatively few studies go on to assess the cost-effectiveness of microfinance interventions relative to other anti-poverty programmes, such as the National Rural Employment Guarantee Scheme (NREGS) or Public Distribution System (PDS). There is also little literature on the extent to which impact studies have influenced policy decisions.

### *Political aspirations*

Rural finance in India cannot be viewed in isolation from the unfolding social transformation initiated by the introduction of universal suffrage more than sixty

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<sup>9</sup> A separate line of research focuses on linkages between microfinance and business training. For example, Ghosh (2002) found the impact of the government TRYSEM programme in West Bengal to be low, whereas Creevey and Edgerton (1997) report positive impact of a World Bank funded pilot in three states. Integrated packages of support to promote dairying, especially for women highlight the importance of quality of intervention to outcomes (Ramakrishnappa & Jagannatha Rao, 2006; Copestake, 1996; Sharma & Vanjani, 1993).

years ago and reinforced by the 1992 constitutional amendment (ratified in 2001) in favour of political decentralization to panchayat institutions. Rao (2009) describes the delegation of decision-making power over public funds to more than one million village panchayats as the largest ever experiment in deliberative democracy in global history. Despite its many flaws, the electoral processes thereby instituted cannot be dismissed as entirely scripted in advance by locally or externally dominant groups. Rao also argues that the immediate well-being outcomes in terms of voice, dignity and influence are less important than expanded reproduction possibilities represented by rising political and material aspirations. This suggests a growing need for institutional mechanisms through which local, state-level and national politicians can respond to these aspirations, and be seen to do so. While transfer programmes (particularly NREGS) have been most in the public spotlight microfinance is significant not only its own right but as a means to improve payment mechanisms for such schemes (CGAP, 2009b). And while failures of implementation reduce immediate material outcomes, a political purpose is nevertheless served if the programmes provide grist to the mill of local and regional political struggles. With respect to microfinance, this constitutes the demand side dynamic to match the supply side proposals on financial inclusion in the Rangarajan report. At the same time anti-developmental, sectarian and Naxalite movements will continue to thrive on aspiration gaps arising from a failure to improve terms of access to financial and other services.

This brief discussion suggests two sets of research questions. The first is to explore positive engagement in the form of direct linkages between financial services and the effectiveness of panchayats within the institutional matrix. Perhaps the leading example here is integration of the SHG network and panchayati raj system through the Kudumbashree programme in Kerala (Ramesh, 2010:3623; Deika & Thampi, 2007).<sup>10</sup> SHGs and their federations also offer a means to increase the density of social networks, communication and transparency (institutionalizing suspicion as well as trust) that is critical to deliberative democratic processes in general, and women's empowerment, in particular (Holvoet, 2005a; 2005b & 2006; Tiwari, 2010). In contrast, Pattenden (2010) labels government and NGO-backed SHGs as a "neo-liberalisation of civil society" that deliver marginal material well-being improvements at best, while ignoring deeper political and economic inequalities and hence the possibility for more radical reproduction consequences. A second and less developed line of research concerns the political inter-relationship between SHGs, NGOs, government schemes and Naxalite activities (Banerjee & Saha, 2010).

More generally, the growing literature on aspirations and poverty, particularly in the face of increased socio-economic flux and complexity affirm the case for researching the diverse "mental models" (North, 1990) that inform how individuals frame and respond to new financing opportunities in the face of pervasive uncertainty. Physical access to microfinance is often less of a constraint to its uptake than basic financial education and socially-embedded

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<sup>10</sup> See also Tesoriero (2006) and Copestake *et al.* (2005:94-125) for further discussion of the links between SHG membership, social identity and active citizenship.

attitudes to saving and borrowing (Nino-Zarazua & Copestake, 2009). This is particularly the case in saturated markets, where stronger NGOs and MFIs can act as catalysts for improving financial literacy and raising the aspirations of previously excluded groups (Narendranath, 2005).

*New information, communication and financial technology.*

New global information, communication technologies and linked financial innovation are partly exogenous to India's well-being regime, but also in part an endogenous response to growing demand for so-called 'bottom of the pyramid' financial services. Such changes are already having profound effects on conventional banks through computerization of back-office activities and the extension of ATM networks (Fu & Polzin, 2008). More far-reaching are prospects for branchless banking, defined by CGAP (2009a:1) as "the delivery of financial services... using ICT and nonbank retail agents, for example, over card-based networks or with mobile phones." The CGAP paper suggests four factors are likely to affect branchless banking worldwide: the changing demographics of users, government regulation, crime and the spread of the internet through data enabled phones. It also suggests that responses will be highly dependent upon country specific factors including competition, the effect of temporary system failures, the evolution of viable business models and relations between regulators, MFIs and mobile network operators. CGAP (2009b) draws attention to another potential driver of change which is the linkage between microfinance and innovation in the way governments make direct payments to poor people both as employees and as recipients of cash transfers, under the NREGS, for example (CGAP, 2009b:6; Adhikari & Bhatia, 2010). Key issues include whether new payment mechanisms can be interlinked with more flexible financial products and services, and how new modalities for making government-to-people or "G2P" payments will affect the messy local politics of patronage that they feed.

Building on pilot activities in the four Southern States, the Rangarajan Committee emphasizes the potential for expansion of the business correspondent model, setting the goal to provide a "BC touchpoint in all 600,000 villages of the country" (Government of India, 2008:52-57). The main objective of this is to facilitate cash transactions, and there has been less discussion of what role correspondents might play in authorizing loans or managing insurance services. CGAP (2009:16) suggests margins for banks and MFIs from such services could quickly fall due to excess demand for reliable agents, prompting some MFIs to concentrate instead on mobile based technology linked to SHGs. Experiences with mobile phones, simplified accounts and smart cards elsewhere suggest an even wider array of possibilities, one driver of which will be the effectiveness of central government to establish a Unique Identification Protocol to enable banks, MFIs, their agents and credit rating agencies to confirm client identity quickly at the point of transaction.

*Climate change and food security*

The core issue here is the adequacy of the matrix of institutions enabling and undermining the efforts of farmers to deal with drought, flood, ill-health and the

perennial need to reconcile seasonal fluctuations in income with daily consumption needs (Swain, 2006; Sawada, 2007). Their effect on poverty is exacerbated by the declining competitiveness of small scale producers, a trend likely to be only partly offset by opportunities for diversification linked to growth in urban incomes (Harriss-White, 2008). Rising world food prices may benefit larger farmers but will exacerbate poverty among the majority of rural inhabitants who are seasonally adjusted net purchasers of food. Meanwhile increasing water supply volatility will induce further changes in cropping patterns and technology, and is likely to accentuate land consolidation, migration and competition over legal and illegal non-farm livelihood opportunities.

Heightened rural livelihood vulnerability has been one factor behind the growing prominence of social protection schemes, including the NREGS (Dreze, 2008), and an important area of research is their integration with microfinance. While “no magic bullet” (Shah, 2008), cash rather than in-kind transfers are less likely to foster dependence if it makes it easier for recipients to save some of the benefits, and indeed borrow against them (see next section). Ray-Bennett (2010) provides detailed case-study evidence of how microfinance can also both support and exacerbate response to major disasters.

Another area of potential innovation in response to increased vulnerability is the provision of micro-insurance. The key issue is how to align products to correlate sufficiently with clients’ actual risks sufficiently to justify them paying a premium sufficient to cover costs of payouts, appraisal and claim management. The leading products are for protection against death and hospitalization particularly in urban areas (Sinha *et al.* 2007; Devadasan *et al.*, 2010; Dror *et al.*, 2009; Ranson, 2002; Ranson, *et al.*, 2007). But India has also been a pioneer in area-based multi-peril crop yield insurance through the National Agricultural Insurance Scheme (NAIS) and its precursors (Mishra, 1996). Linked to seasonal crop loans, the NAIS covers more than one in ten farmers in the country (Nair, 2010:2) making it the largest crop insurance in the world, although also one of the most heavily subsidized (Mahul & Stutley, 2010:108). Weather index linked insurance has been much touted as an alternative (Mosley & Krishnamurthy, 1995) that can also be packaged with credit. But its effectiveness is constrained by access to sufficiently fine-grained meteorological data, as well as the challenge of tailoring and marketing of products to match the highly diverse risk profiles of different categories of farmer (Gina *et al.*, 2007; R.Nair, 2010a; 2010b).

Microfinance also needs to be analysed in conjunction with finance for collective infrastructure investments capable of crowding in private investment in livelihoods by enhancing their profitability and reducing their susceptibility to climate change. Such activities include irrigation, erosion control, flood defence, social forestry and applied agronomic research and technology development. Nino-Murcia (2006) suggests that returns to investment in social forestry can also be very high. Yet public investment programmes, like NABARD’s Rural Infrastructure Development Fund, have attracted little independent research and evaluation (Chandrasekhar & Ray, 2005:22). SHG federation can help to build capacity for collective action (Ramesh, 2007), but individual loans may also

weaken incentives to collective investment, as in the case of groundwater over tank irrigation. Unfortunately, research into interactions between private investment and collective watershed development on rural livelihoods and well-being outcomes is again scarce (exceptions include Srinivas & Rao, 1998; Reddy *et al.* 2004).

A linked and growing issue is the role of rural finance in aiding efforts to reduce India's contribution to climate change carbon equivalent emissions. These include mechanisms to finance renewable energy production in the form of biofuel, wood, biogas, solar and wind, as well as to pay farmers for fixing carbon through agro-forestry, with possible new sources of international finance under the Clean Development Mechanism, REDD+ and related initiatives (World Bank, 2010:258; Singh, 2008). In addition to evaluating the impact of such programmes research is needed into the relative effectiveness of different configurations of state, market and civil society in the management of commons, such as hill forest tracts (Baland *et al.*, 2008).

#### **4. Research priorities and methodologies**

Recent literature on the methodology of microfinance research has centred on how to arrive at more reliable estimates of impact. Most of the impact studies reviewed in the first part of the last section relied on quasi-experimental designs that at best imperfectly raise questions about the extent to which they remain subject to selection and other biases. A leading response to these difficulties has been increased use of randomized control trials (CGAP, 2010; Duflo, 2006; Banerjee *et al.* 2009; Copestake, 2011). RCTs offer a robust solution to the selection bias problem, and the practical implications of the findings they generate can often be more easily interpreted than those produced by quasi-experimental designs. However, doubts persist over the range of problems they can be applied to, their cost, ethics and external validity (Ravallion, 2009; Rodrik, 2008; Copestake *et al.*, 2009). Both Rodrik (2008) and Deaton (2009) argue strongly that quantitative research should not be carried out solely for the purpose of impact assessment, but also to test and extend relevant theory so as to inform decisions over the role of rural finance in contexts that can never precisely replicate those subjected to primary research. This highlights the importance of combining quantitative research with qualitative methods designed to cast light on impact heterogeneity and causal pathways, including unintended outcomes and how financial and other 'treatments' interact.

Table 1 contrasts this narrower instrument-specific and policy-oriented research with broader and more open-ended research suggested by the well-being framework presented in Section 2. The narrower agenda is more likely to be associated with quantitative impact assessment. It is also more amenable to systematic review and meta-analysis. Conversely, the broader agenda lends itself to qualitative methods more able to accommodate the role of microfinance as one component of complex systems and processes with uncertain and system level outcomes. Village level studies, for example, help to highlight the extent to which financial relations remain embedded in deep structures of inequality

(Ramakumar, 2006; Harriss *et al.*, 2010) and to reveal the combined effect of microfinance on the local economy (Mitra, 2007). However, this association between responses and methodologies is far from perfect: qualitative research is important to framing the narrower agenda, and statistical data is also important to the broader agenda. For example, large household surveys remain important as a means to monitoring the relative importance of different forms of microcredit and debt by region and socio-economic group (Kalamkar, 2005).<sup>11</sup>

**Table 1. Narrower and broader research agendas**

Driver of change	NARROWER Policy-specific or instrument oriented research.	BROADER Open-ended or naturalistic research.
Evidence led policy reform	Impact and cost-benefit studies.	Political economy of policy processes.
Popular aspirations and political responses.	Incorporate a wider range of aspiration variables.	The indirect effects of finance on processes of social mobilization and public action.
Organizational responses to technological change	Evaluation of supply-side financial effects of product and process innovation (e.g. branchless banking) and impact assessment of their effects on client outreach and impact.	Changing landscapes of informal and formal finance, including cultural and sociological ramifications of ICT on institutional interactions and personal financial management practices of poor people.
Food insecurity and climate change	Uptake and impact of policies and programmes to promote increased output, food security, adaptation to climate change (e.g. weather insurance) and climate change mitigation.	The indirect effects of finance on individual, household and community level coping strategies and livelihood adaptation, including socio-economic differentiation.

The distinction between narrower and broader research perspectives spans not only that between quantitative and qualitative methodologies, but also contrasting mental models of microfinance. Gravesteyn and Copestake (2010) distinguish between three such models: “business first”, “development first” and an intermediate “social enterprise” model. Within the first, a narrower research perspective would focus on the profitability of both providers’ and users’

<sup>11</sup> Quantitative studies of well-being outcomes as diverse as contraceptive use, child labour use (Sawada, 2006), crop and livelihood diversification (Sarkar, 2007; Sharma, 2007; Sidhu, 2006), and rural non-farm income (Toor, 2006; Micevska & Rahut, 2008) can produce evidence of possible wider effects of credit constraints.

businesses. But a business first perspective is also more broadly concerned with meso-level and macro-level financial market integration, deepening, innovation and regulation. Likewise the development first model encompasses both a narrower concern with the impact of microfinance on poverty and a broader concern with how this contributes to well-being outcomes at the meso and macro-level, by supporting more inclusive growth, for example. Third, the social enterprise model is concerned with both the technical feasibility of double-bottom line management in MFIs and with the broader political economy of 'third way' strategies for balancing financial and social goals at the sector level (Copestake, 2007).

The distinction between narrower and broader research agendas maps more closely onto different ways of thinking about the management of development. The narrower agenda is more congruent with viewing microfinance as a potential tool for rational implementation of policies of livelihood development, poverty reduction and so on. In contrast, the broader agenda can embrace research into microfinance as the instrument of ruthless capitalists, corrupt public officials and so on. Gulrajani (2009) seeks to break the impasse between these "new public management" and "critical management studies" perspectives by pointing out the possibility of a "non-managerialist romantic development management" practice. This places complexity, uncertainty and diversity of interests at the centre of development, along with deliberative but unavoidably messy political processes of framing and instituting actions. While unable to reconcile all differences this approach at least recognizes and attempts to respond to some of them consensually. At one extreme there is a danger of focusing too narrowly on policy-driven impact assessment at the risk of being co-opted into predetermined ideological visions of what microfinance should be and could be about. But at the other extreme there is a danger of focusing too broadly on political economy and foregoing opportunities to institute more immediate and systematic positive change.

To conclude, this paper has used a well-being regime framework to define development in a sufficiently broad way to embrace research into microfinance both *in* development and *for* development. The broad survey of literature on rural microfinance in India has highlighted the value of diversity of analytical and methodological approaches to our understanding of the complexity of its relation to development thus defined. This has led us to warn against an exclusive focus on policy-oriented impact assessment, for fear of crowding out complementary research into the adaptive response of microfinance and other forms of rural finance to challenges posed by other conditioning factors (including rising political aspirations, technological innovation and climate change). In this respect, the well-being regime framework employed is located firmly in the broad and policy-relevant, but not policy-driven, interdisciplinary tradition of development studies.



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